

NEW MARKET ASSESSMENT STRATEGIES

March/April 2006
Number 2 Volume 2



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Are Your Investors Nervous?

Is Your Big Project Stalled? What You Should Do About It Now?

Familiar Scenario? Your luxury condo project is stalled because key investors are worried about getting an adequate return if housing prices slump over the next few years. “Push it back,” say the investors, that is, when you can actually get them to sit down and talk about the problem. “Cut back on the design, tone down on luxury features. We’ll reduce the price point and build next year.”

You’re concerned about delays too because financing costs for land acquisition and pre-construction activity already cost you a cool million dollars a month. And you haven’t even broken ground yet. What can you do? What are you going to tell your nervous investors to get the project moving again?

Investor paralysis is rising as many developers struggle with overbuilt markets, rising interest rates, and uncertain buyers. Because they’re not sure if new projects being planned or under development now will sell at desired prices in 2-3 years, many developers are doing nothing; it’s called “developer paralysis.” And it’s a growing problem among companies that don’t yet have the deep insight that rigorous market analysis and risk management can give.

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Market Bubble or Housing Hysteria?

The New Math of High-End Real Estate Markets

Two California economists, Gary and Margaret Smith, spend a lot of time thinking about real estate: their own, and your’s too. By applying econometric tools, innovative thinking, and rigorous mathematical analysis to the top US markets, they have found that higher-end properties in Los Angeles, New York, Miami, Chicago and most other “bubble” real estate markets aren’t overpriced. In fact, all but a very few locations are substantially undervalued.

When viewed from a quantitatively-focused “economist” perspective, the resulting analysis shows that while most of today’s affluent real estate markets may look like a price bubble, they really aren’t. These studies show that higher-end residential properties, especially luxury condos, are probably underpriced by about 15-20%, particularly in the three most desirable, expensive cities: LA, New York, and Miami. And even more in places like Atlanta and the heartland.

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“After New York and California, South Florida has become the most desirable and productive real estate market in the country.”

Real Estate Market Trends

Looking Ahead: Selected 2007-2009 High-End Real Estate Markets

What's really happening in luxury real estate markets now? What is likely to occur over the next 2-3 years? Are the headlines and financial prognosticators accurately predicting key market trends? Is the bottom about to fall out of the high-end condo boom? Or is today's rising doom & gloom in "hot" real estate locations fueled more by "wall-of-worry" hysteria than by sound data and insightful analysis?

While predicting the future is always risky, what we're not finding among the more informed participants in real estate markets is confusion, fear, or hesitation. The reason is simple.

Luxury buyers are continuing to invest aggressively in the most desirable locations: New York, Los Angeles, and South Florida. The affluent are economically savvy; they are making that next luxury home purchase now to lock in a lower interest rate. There are also more millionaires looking for luxury properties than ever before, 8.9 million in the US alone. And when you include the affluent abroad, the numbers of potential buyers of luxury properties outstrips even the last ten boom years. Sellers also know that prices are still rising, just at a slower pace than last year.

Sure, interest rates are higher than two years ago, but historically not by that much. And while the Fed is expected to bump the prime up a few more times this year, it doesn't quite have the limiting power it once did. An ever-increasing array of financing options, including sophisticated asset management, and flexible mortgages has fundamentally changed the way affluent buyers acquire second homes.

But the affluent are not only buying larger, more luxurious homes, they're buying more of them. A fast growing trend among the almost 9 million US millionaires is the 2-condo household - one at home for summertime and family; the other in South Florida for winter, golf, and friends. Where are they buying? After New York and California, South Florida has become the most desirable and productive real estate market in the country.

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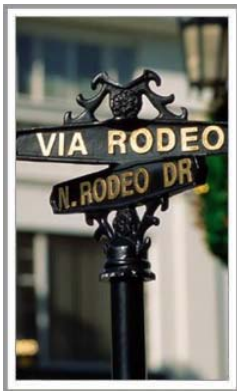
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Better information leads to more informed choices and better decisions. And better data starts with a quantitative market assessment. It is a critical factor in getting the highest return on future real estate development investments.

Data driven market analysis is the norm in virtually every other industry. Real estate has lagged because it has been a local, smaller-scale industry for so long. But as consolidations, mergers and mega-projects increase, it is becoming critically important to get the highest, fastest return on investments in luxury real estate developments.

Incorporating a PMCA Market Assessment into the project cycle early can materially reduce "developer paralysis" and risk, help you focus Marketing & Sales strategies, lead to increased buyer satisfaction, shorten the sales cycle, and improve ROI. #

"Deeper economic analysis indicates that the best measure of true real estate valuation and future pricing trends actually lies in the rents that markets can command."



Ambiance and amenities matter a lot to the affluent buyer. Defining and delivering these more cost-effectively will be key to successful high-end property development

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Real Estate Isn't Local Anymore

CNN reports that “million dollar-plus properties (homes and condos) is now the strongest segment of many housing markets.” In Southern and Midwestern markets \$500,000 will buy you a pretty nice home; but in the hottest markets such as Miami, you are looking at an efficiency condo. Affluent buyers won't settle for that; they want luxury with a capital “L.” And they aren't just from the usual domestic wealth segments either. Wealthy buyers now come to the top US locales from new “hotspots” - China, India, Korea, Australia, and the Middle East. After New York and California, South Florida has become the most desirable and productive real estate market in the country.

Internationally, hundreds of thousands of successful entrepreneurs, professionals, and business owners from both the US and abroad are acquiring second and even third homes in the top US markets. With attractive incentives ranging from greater purchasing power and tax advantages back home, to the desire for safe havens and even American citizenship, foreign buyers now account for as much as 30-40% of high-end residential purchases in the major coastal markets of NY and CA.

Condo ‘Glut’ or Sales Pause?

In two key real estate markets, New York and Miami, developers have over the past five years constructed a record number of new units, and some analysts are now concerned that these locations are severely overbuilt with expensive condos and townhouses. The resulting price declines will, they say, likely depress these premier markets for the next 5-8 years or more. Other, more globally astute analysts disagree, pointing out that the worldwide demand for affluent lifestyles, and the residential properties that complement those lifestyles, is only going to increase as more nations become successful market economies.

In both of these high-end real estate markets, condo sales remain brisk at the high end because the type of buyers has begun to rapidly change. As China, India and other centers of wealth rise, the newly-affluent will join other international investors and acquire luxury properties in the most desirable US markets. Over the next decade, we should expect demand for thoughtfully designed and culturally diverse properties to grow at a projected 10-15% annual pace.

It is increasingly likely that the current slowdown in sales of luxury condos in some markets is due, at least in part, to a significant change in buyer profiles. What has been successful over the past decade isn't any longer because the affluent buyer is now coming to the top US real estate markets with different needs. As developers begin to understand their new customers and adapt product and services, sales activity will resume.

The Long Boom

The world wide demand for luxury properties in top US locales is starting to resemble the Japanese Invasion of the 1980's, but this time, it's likely to last for years. Back then, flush with dollars; international investors (not just the Japanese) went on a buying binge that is still echoing some 25 years later. This time around, it's bigger: China, India, and the rest of Asia Pacific. And the New Europe, Russia, and the oil-rich Middle East aren't far behind. As today's real estate “bubble” hysteria subsides over the next couple of years, demand for high-end real estate in New York, Los Angeles and Miami will certainly resume its torrid pace.



NY, CA & FL are the top luxury condo buying markets and show little sign of slowing down over the next 5 years. But the kinds of units and amenities that buyers want are changing.

“A quantitative market assessment is a critical factor in getting the highest return on future real estate development investments.”

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This new real estate assessment approach points out that the true value of higher-end properties is better revealed by understanding the relationship between what similar properties in the same market rent for. Calculate the future rents, subtract mortgage payments, taxes and other costs, factor in a good annual rate of return of 6% or more, and then you are looking at the proper price of a home or condo in today's real estate markets.

Speculating about real estate bubble occurs whenever there is a rapid increase in asset prices. Robert J. Schiller, the Yale economist noted for a decades-long bearish viewpoint, agrees that this new approach is worth considering because "it emphasizes the link between home prices and rent as the way to understand the value of real estate."

Traditional housing surveys use the relationship between prices and income to determine if we're in a market "bubble." It's simple and easy to understand. But it's also wrong; say a growing number of economists, who are quick to point out that this older approach doesn't yield that much usable insight about real estate trends or explain why current housing prices are high, especially where local and national markets are in transition.

Better Housing Math

The current housing valuation model involves looking at "comps" as if real estate was stock: similar to "thinking Yahoo is a bargain at \$32 a share because Google is selling at \$390 a share." As with equities, you need to understand the relationship between price and future earnings.

For housing, particularly high-end properties, you need to know how the current price relates to the future stream of rent income, whether you plan to rent or not. Once that relationship is grasped, today's high prices don't seem that outrageous. In fact, the Smith's argue that for the high end of the residential condo market, most properties are still undervalued.

Buyers must now consider two scenarios when deciding to purchase in today's markets: the first is that you buy and the price goes down. The second is that you don't buy and the price goes up. Dr. Smith points out that the second is scarier.

What Bubble?

What if the price of a luxury condo or townhouse drops in the next year or two? That, of course, is the risk in owning over renting. If buyers try to "time" the real estate market, they are probably going to experience the same dismal rate of return experienced by most who try to market-time equities. If they wait for prices to drop, they will pay less and get a better ROI. But waiting may also lock them out of a rising market later on. That's the reason it's so important to analyze the fundamentals - using more than a simplistic "comps" approach. If buyers and developers alike compute a healthy return and hold real estate investments for the longer term, they minimize the risk of loss and maximize ROI.

Compare the present real estate climate, if you will, to the dotcom bubble of the late 1990's. When Internet stocks pushed the equities markets to record highs, analysts tried to explain valuations by talking about how the Web was creating a "new" global economy, one that worked by different rules based on viewership and not earnings. It was smoke & mirrors.

Now, effective valuations for stocks once more depend on careful analysis of the fundamentals, and not on market hysteria. The same reasoning applies to luxury real estate. The real value in the Smith's research may lie in its practicality. It focuses on how valuations are determined, not on why prices may be high. It promises a better way for developers, investors, real estate brokers, financial planners, sellers and buyers to understand how much is too much to pay for high-end residential properties.

"In Southern and Midwestern markets \$500,000 will buy you a pretty nice home; but in the hottest markets such as Miami, you are looking at an efficiency."

Today's Market Assessments

Why 'Business as Usual' Isn't Enough Anymore

Build it and they just might not come. Not if your project fails to appeal to the new waves of international investors, buyers who now account for as much as 30-40% of higher-end condo sales in places like New York, LA, and Miami.

What has worked in past real estate "feeding frenzies" doesn't always prove reliable when the tide changes. Business isn't "usual" anymore. Sales activity has slowed, core inflation and Fed rates are both rising, and Fear, Uncertainty & Doubt (FUD) are being stirred up by constant newspaper and television coverage of the "Housing Bubble."

Changing Market Dynamics

Uncertain economic conditions, changing buyer needs or different cultural preferences, and the entry of new kinds of affluent customers will require a greater flexibility in how real estate developments are put together - as well as more rigorous, quantitative analysis before you design and build.

Many real estate and financial experts believe that the years ahead will demand greater sophistication in the ways that developers conceive, plan and execute future projects. The days of "seat-of-the-pants" builder, informal project financing, and "super-hot" seller's markets is rapidly slip-sliding into history.

Business Value of Better Information

Today's Market Assessment should include more than local or regional market data and analysis; buyers of luxury properties are increasingly global. It should provide local comparative data, but match that with regional, national and selected international market information because that's where tomorrow's affluent buyers are coming from.

A market assessment is crucial to the development of an effective marketing & Sales strategy, and it should be completed well before these are created. It should also provide insight into who likely buyers might be and how they can be reached.

Better, more economically-sound, data driven market analysis will be, as it is in virtually every other industry, a critically important factor in to getting the highest, fastest return on investments in tomorrow's luxury real estate developments. Incorporating a PMCA Market Assessment into the project cycle early can materially reduce risk, help you focus Marketing & Sales strategies, lead to increased buyer satisfaction, shorten the sales cycle, and improve ROI.

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New Market Assessment Strategies is a bi-monthly real estate market assessment newsletter produced by PMCA for its clients.

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